

CALIFORNIA LOTTERY

Audit Report

3 BALL PRODUCTIONS/MILESTONE ENTERTAINMENT CONTRACT

August 1, 2008, through June 30, 2010



JOHN CHIANG
California State Controller

May 2011



JOHN CHIANG
California State Controller

May 18, 2011

John Mass, Chairperson
California Lottery Commission
600 North Tenth Street
Sacramento, CA 95811

Dear Mr. Mass:

The State Controller's Office audited the California Lottery's (Lottery) 3 Ball Productions/Milestone Entertainment contract for the period of August 1, 2008, through June 30, 2010.

Our audit disclosed deficiencies in the Lottery's fiscal controls over payments and its monitoring of the contract. The Lottery improperly overpaid an advance payment and lacked support for contract expenditures. In addition, a contract payment was made before the amendment authorizing additional funds was executed, and also failed to follow approved competitive bidding guidelines. Furthermore, the Lottery improperly used the revolving fund for contract payments that should have been processed through the normal claim process, and did not consistently perform payment reconciliations.

If you have any questions, please call Andrew Finlayson, Chief, State Agency Audits Bureau, at (916) 324-6310.

Sincerely,

Original signed by

JEFFREY V. BROWNFIELD
Chief, Division of Audits

JVB/vb

cc: John Menchaca, Commissioner
California Lottery Commission
Alex E. Fortunati, Commissioner
California Lottery Commission
Linh Nguyen, Acting Director
California Lottery
Michael Brennan, Deputy Director
Sales and Marketing Division
Michael T. Ota, Deputy Director
Finance Division
California Lottery
Roberto Zavala, Chief
Internal Audits
California Lottery

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Audit Report

Summary

The State Controller's Office (SCO) audited the California Lottery's (Lottery) 3 Ball Productions/Milestone Entertainment contract for the period of August 1, 2008, through June 30, 2010.

Our audit disclosed the following deficiencies in the Lottery's fiscal controls over payments and its monitoring of the 3 Ball Productions/Milestone Entertainment contract. The Lottery:

- Improperly overpaid an advance payment and lacked support for contract expenditures;
- Made contract payment before an amendment authorizing additional funds was executed;
- Failed to follow approved competitive bidding guidelines;
- Improperly used the revolving fund; and
- Did not consistently perform payment reconciliations.

Background

By authority of the California Constitution, Government Code section 12410 states, "The Controller shall superintend the fiscal concerns of the state. The Controller shall audit all claims against the state, and may audit the disbursement of any state money, for correctness, legality, and for sufficient provision of law for payment." In addition, Government Code section 12411 stipulates that "... the Controller shall suggest plans for the improvement and management of revenues."

Proposition 37, the California State Lottery Act of 1984 (Lottery Act), amended the California Constitution to authorize the establishment of a statewide lottery, to create the California Lottery Commission, and to give the commission broad powers to oversee the operation of a statewide lottery.

Pursuant to Government Code section 8880.46.6, the SCO may conduct other special post-audits of the Lottery, as the State Controller deems necessary. The Controller or his/her agents conducting an audit under this chapter shall have access and authority to examine any and all records of the California Lottery Commission.

The Lottery entered into a contract with 3 Ball Productions/Milestone Entertainment (contractor) to provide:

- Creative and broadcast production services in connection with a weekly lottery-based series titled "Make Me A Millionaire";
- Staff sufficient to perform contract-related services;
- Set design and maintenance of studio space and equipment;
- Closed captioning services; and
- Other services specified in the contract's Scope of Services.

The original contract is for the period of August 1, 2008, through July 31, 2012, with an option for the Lottery to extend it for up to two additional years. The maximum obligated amount of the original agreement is \$14,000,000. Since the contract was initiated, there have been three amendments, as follows:

- Amendment A01—To memorialize the working agreement dated November 7, 2008, between the Lottery and the contractor and (1) deletes the requirement for fidelity bonds or crime/employee dishonesty insurance, and (2) amends the amount of financial security for the Lottery.
- Amendment A02—To incorporate modified language pertaining to Contract Terms and Conditions, section 5.2, Frequency of Payment, section 5.3, Payment, and to Attachment 1, Cost Sheet section I, A3, and section I, B.
- Amendment A03—To increase funding by \$356,000 and modify language pertaining to Exhibit A, Scope of Services, and Attachment 1, Cost Sheet. The maximum agreement amount after the amendment increased from \$14,000,000 to \$14,356,000.

Subsequent to our audit period ended December 31, 2009, on April 30, 2010, the Lottery notified the contractor that, contingent upon Lottery Commission approval, the Lottery intended to terminate the contract. On June 25, 2010, the Lottery Commission approved the termination of the contract.

Objectives, Scope, and Methodology

We conducted this performance audit in accordance with generally accepted government auditing standards. We did not audit the Lottery's financial statements. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

This audit was performed to determine whether the Lottery's fiscal controls over the monitoring of the 3 Ball Productions/Milestone Entertainment contract were adequate and whether contract payments made by the Lottery were legal and proper.

The specific objectives of the audit were to determine whether the Lottery ensured that:

- Contract payments were legal and proper;
- Internal controls are adequate and in compliance with the terms and conditions of the contract;
- The contractor abided by state laws, rules, regulations, and policies with regard to its contract performance; and
- The contractor provided the Lottery with specified deliverables according to the terms and conditions of the contract.

The procedures performed during the audit included:

- Reviewing the contract and subcontracts, contract law, regulations, rules, Lottery policies, and related accounting records;
- Reviewing work performed by any external audit organization or by any other Lottery unit relevant to the contract;
- Obtaining an understanding of components of internal controls sufficient to conduct the audit;
- Interviewing and observing individuals involved in the development, authorization, and monitoring of the contract; and
- Performing tests of procedural compliance and tests of payments, in the administration of the contract.

Subsequent to our audit period ended December 31, 2009, the Lottery Commission approved the termination of the 3 Ball Production/Milestone Entertainment contract on June 25, 2010, thereby cancelling the “Make Me a Millionaire” TV game show. We expanded our scope for the period of January 1, 2010, through July 30, 2010, and the expanded scope included, but was not limited to, the following procedures:

- Reviewing the contract and subcontracts, contract law, regulations, rules, Lottery policies, and related accounting records;
- Reviewing work performed by any external organization or by any other Lottery unit relevant to the contract;
- Interviewing and observing individuals involved in the authorization, and monitoring of the contract; and
- Performing tests of procedural compliance and tests of payments, as we deem necessary.

The objectives of the audit included, but were not limited to, determining if:

- The Lottery abided by state laws, rules, regulations, and policies with regard to the contract;
- The Lottery had plans to ensure the continuance of the TV game show;
- The Lottery had any plans for the disposition of any assets purchased through the contract if the TV game show was cancelled; and
- The contract payments were legal and proper.

Conclusion

Our audit disclosed deficiencies in the Lottery's fiscal controls over payments and its monitoring of the 3 Ball Productions/Milestone Entertainment contract. The Lottery:

- Improperly overpaid an advance payment by \$1,187,019 and lacked support for contract expenditures totaling \$29,350 (Finding 1);
- Made a contract payment of \$300,000 before the amendment to authorize additional funds was executed (Finding 2);
- Failed to follow approved competitive bidding guidelines for two purchases of more than \$100,000 (Finding 3);
- Improperly used the revolving fund for contract payments totaling \$357,324 that should have been processed through the normal claims process (Finding 4); and
- Did not consistently perform payment reconciliations (Finding 5).

**Views of
Responsible
Official**

The SCO issued a draft to the Lottery dated February 25, 2011. Linh Nguyen, Acting Director, responded by the attached letter dated March 24, 2010. Mr. Nguyen agreed with Findings 1, 2, 4, and 5, but respectfully disagreed with Finding 3.

Restricted Use

This report is intended for the information and use of the California Lottery, the California Lottery Commission, and the SCO; it is not intended to be and should not be used by anyone other than these specified parties. This restriction is not intended to limit distribution of the final report, which is a matter of public record.

Original signed by

JEFFREY V. BROWNFIELD
Chief, Division of Audits

May 18, 2011

Findings and Recommendations

**FINDING 1—
The Lottery improperly
overpaid an advance
payment and lacked
support for contract
expenditures.**

Our audit disclosed that the Lottery overpaid an advance payment by \$1,187,019, the excess of the amount allowed by the contract. In addition, the Lottery did not have adequate support for contract expenditures totaling \$29,350.

We tested 35 out of 72 invoices (48.61%) submitted for payment by 3 Ball Productions/Milestone Entertainment (contractor) to the Lottery and identified the following discrepancies:

- The Lottery made an advance payment to the contractor in the amount of \$2,967,548, which represented 100% of the estimated costs including mark-up, for an LED screen and other game set pieces and design for the TV game show “Make Me a Millionaire.” The advance payment amount should have been only \$1,780,529 (60%), as allowed by the contract. Therefore, the Lottery over-advanced \$1,187,019 to the contractor.
- In addition, \$17,263 could not be supported by subcontractor’s invoices (\$2,717,949 – \$2,700,686).
- The Lottery paid the contractor’s invoice, totaling \$50,000, for lighting for the TV game show. However, the Lottery could provide support for only \$37,913 of the subcontractor’s invoice and could not support the remaining \$12,087. After the SCO auditors made the contract manager aware of the difference, on June 2, 2010, the Lottery contract manager disputed this invoice to adjust the overpaid amount of \$12,087.

Contract No. 12892, section E, Set Design, Procurement, and Maintenance, on page 8, states:

The Lottery agrees that, with respect to necessary design and building of the sets to be used for the Series, upon presentation to Lottery of acceptable documentation evidencing: (a) the contractual requirement of advance payments to subcontractor(s); and (b) the actual costs for such Build-out, the Lottery shall advance Contractor up to 60% of the budgeted Build-out costs.

The Contract Manager’s Handbook, dated June 2007, Chapter 4, Invoice Process, page 16, specifies the following action steps to be taken by the contract manager before approving and forwarding invoices to the Accounting Operations and Prize Payment (AOPP) Bureau (formally Accounting Operations and Tax Bureau) for payment:

- Review all invoices for accuracy. Verify that the services/equipment have not previously been billed. Cost rates are limited to those specified in the contract. Check all mathematical calculations for accuracy.
- Certify that the work or service which was billed for was performed and goods were received and that the amount payable is correct and is billed in accordance with the terms of the contract.

The Lottery contract manager did not obtain and review supporting documents for those two invoices until auditors asked to examine those documents. According to the Lottery's AOPP Bureau, the contract manager approved and released the full amount in the accounting system to process the payment. Advancing payments to the contractor at a percentage that exceeded the terms of the contract increased the chance of the Lottery overpaying the actual costs incurred by the contractor. In addition, the Lottery might have advanced payments for goods and services that may not have met the Lottery's requirements and standards.

Failure to review invoices for accuracy reflects weak control over contract payments.

Recommendation

The Lottery should properly verify contract expenditures to the contract's terms and conditions to ensure advance payments are made at the percentage allowed. In addition, the Lottery should recover any payments that were not adequately supported. In the future, the Lottery should obtain and review supporting documentation to ensure expenditures are proper and accurate before payments are processed.

Lottery's Response

The Lottery agrees with the finding and took immediate corrective action in July 2010 by assigning a new contract manager and emphasizing internal controls over contract payments. Currently, contract expenditures are verified to contract terms and advance payments are made at the percentage allowed. The Lottery initiated a formal dispute on unsupported costs and will seek to recover disputed payments.

SCO's Comment

The Lottery concurs with the finding and recommendation.

**FINDING 2—
A contract payment
was made before the
amendment authorizing
the additional funding
was executed.**

Our audit disclosed that a payment totaling \$300,000 was made to the contractor for additional production costs before the amendment to authorize the additional funds was executed. The Lottery received the invoice dated April 26, 2009, and scheduled the payment on June 9, 2009. Four months later, on September 24, 2009, Amendment A03 for the authorizing additional funding was executed. As the amendment had not been executed at the time of the payment, the Lottery improperly paid for work that was outside of the payment provisions of the contract.

The Contract Manager's Handbook, dated June 2007, Chapter 7, states:

Amendments must be requested and dated prior to the date the amendment is to take effect. To the extent possible, the Contract Manager must plan for amendments at least five months in advance of the needed change. Contract Managers cannot authorize additional work or expenses until the amendment is fully executed. Accounting cannot legally pay for any work performed through an amendment before its execution.

The Lottery contract manager overseeing the contract informed the SCO auditors that payment was processed before the amendment was executed because of the contractor's immediate need for additional production costs.

Recommendation

The Lottery should not authorize additional contract work or expenses until a contract amendment is fully executed. The Accounting Operations and Prize Payment Bureau should not pay for any work performed except as authorized under the contract.

Lottery's Response

The Lottery agrees with the finding and will ensure that future contract work or expenses are not authorized until a contract amendment is fully executed. In addition, the Lottery will ensure payments are made for work performed under the contract.

SCO's Comment

The Lottery concurs with the finding and recommendation.

**FINDING 3—
The Lottery failed to
follow approved
competitive bidding
guidelines.**

Our audit disclosed that the following two purchases of more than \$100,000 were not properly processed through the Lottery's approved competitive bidding guidelines as required by the contract. In addition, no memorandum was prepared to the Chairman of the Commission to explain why these purchases were exempted from the competitive bidding process.

- \$817,699 was an accumulation of many purchases for game set pieces and design
- \$275,000 was paid for set lighting design and programming

Regarding the first purchase for game set pieces and design, on June 3, 2010, the Lottery provided the auditors with a letter dated October 30, 2008, prepared by 3 Ball Productions/Milestone Entertainment. This letter explains the justification for being exempted from using the competitive bidding guidelines in the work of building sets for the Lottery's TV show. However, the letter was not brought to the director's attention, nor did the director prepare a memorandum explaining this circumstance to the Chairman of the Commission. For the second purchase for lighting design and programming, there was no written justification provided for exemption from the competitive bidding process.

Contract No. 12892, section E, page 8, states:

The Contractor shall procure all set pieces and potentially some draw devices (if and as required by the Lottery) for the Series using the Lottery's Approved Competitive Bidding Guidelines.

The Lottery Regulations, Section III.E.,S, Competitive Bidding Procedures, dated December 3, 2008, page 109, specifies:

These [competitive bidding] procedures are adopted pursuant to Government Code section 8880.56(b) (1) which requires the California State Lottery Commission to "...adopt and publish competitive bidding procedures for the award of any procurement or contract involving an expenditure of more than one hundred thousand dollars (\$100,000). . . ."

For exemptions from the competitive bidding procedures, California Lottery Regulation, page 110, requires that "the Director shall prepare a memorandum explaining the applicable circumstances and shall provide written notice to the Chairman of the Commission."

The Lottery's contract manager explained that there was no competitive bid for these purchases due to time constraints, and because the contractor had the expertise and knowledge about the industry to bring the Lottery the best prices.

Failure to use competitive bidding procedures for purchases of more than \$100,000 could result in the Lottery not receiving the best prices for goods or services.

Recommendation

The Lottery should properly oversee contracts by monitoring the competitive bid procedures for purchases of more than \$100,000. These procedures are designed to ensure that the Lottery gets the best price possible. In addition, if the Lottery does not use the competitive bidding process, the director must prepare a memorandum explaining why the competitive bidding process is not being used, and send it to the Chairman of the Commission.

Lottery's Response

For clarification, the Lottery's competitive bidding guidelines allow the Director and prime contractors to procure goods or services without utilizing competitive procedures if the goods or services are being acquired through a subcontract to a competitively bid prime contract that identified the goods or services at the time of prime contract award. The scope of services in the Request for Proposal for the "Make Me a Millionaire" game show required the contractor to provide studio equipment and a set design including the procurement of game set pieces and lighting. Because the studio equipment and set design are part of the prime contractor's scope of work, the Lottery considers that the game set pieces and lighting to have been competitively bid by the prime contractor, in accordance with the Lottery's competitive bidding regulations.

The Lottery's competitive bidding guidelines are complex and are relevant only in the context of a state-operated lottery. To ensure a consistent application of its guidelines the Lottery will provide consultation and training to contract managers as needed to ensure its guidelines are followed. Based on this clarification, the Lottery respectfully disagrees with the finding.

SCO's Comment

The Lottery should have followed the competitive bidding procedures for goods and services procured through subcontractors. The goods and service were not identified at the time the prime contract was awarded. The specific goods and services or costs were not identified in the scope of services in the Lottery's Request for Proposal for the "Make Me a Millionaire" game. In addition, the contractor's response to the Request for Proposal did not include a specific description of or costs of the game set pieces and lighting, nor did it identify the subcontractors. Not following its own competitive bidding guidelines puts the Lottery at risk of not receiving the best value for goods and services procured through subcontractors. The finding remains unchanged.

**FINDING 4—
Improper use of the
office revolving fund**

Our audit disclosed that the Lottery improperly used the office revolving fund to pay for contract expenditures totaling \$357,324. These expenditures should have been paid through the normal claim processing procedures and a State Controller's warrant issued.

The following expenditures were paid through the office revolving fund:

- \$201,500 was paid for production and creative service costs and \$81,673 was paid for talent costs.

The SCO auditors were informed by AOPP Bureau staff that the two invoices were paid through the revolving fund because the contractor requested immediate payment due to its business nature and to meet its payroll deadline. However, there is no provision in the contract that allows for early payment based on the contractor's financial needs.

- \$73,827 was paid for talent costs and \$325 for wardrobe costs.

The two invoices were dated July 31, 2009, but were not processed for payment by the AOPP Bureau until August 25, 2009. The contract manager and bureau staff could not provide evidence explaining the delay and for not processing the payment through the normal claim process.

State Administrative Manual (SAM) section 8110 states that:

Revolving funds drawn under the provisions of Government Code section 16400 may be used only, in accordance with law, for payment of compensation earned, traveling expenses, traveling expense advances, or where immediate payment is otherwise necessary (Government Code section 16401). In determining whether immediate payment is necessary, the determining factor is whether payment could be made through the normal claim processing procedure and a State Controller's warrant issued.

The improper use of the office revolving fund may cause misuse of State funds for expenditures that are not allowable.

Recommendation

The Lottery should only use the office revolving fund process for purposes as delineated in SAM, and payment of contract expenditures should be paid through the normal claim processing procedure and a State Controller's warrant issued.

Lottery's Response

The Lottery agrees with the finding. The Lottery will comply with its existing payment procedures by processing claims through SCO for contract expenditures and will use the office revolving fund in accordance with SAM guidelines.

SCO's Comment

The Lottery concurs with the finding and recommendation.

**FINDING 5—
Payment reconciliations
were not performed
consistently.**

Our audit disclosed that the Lottery did not perform quarterly reconciliations between the Lottery contract manager's payment records and the official accounting records for the quarters ended December 31, 2008, March 31, 2009, June 30, 2009, and September 30, 2009. However, the Lottery did perform reconciliation for the quarter ended December 31, 2009. According to the Lottery's AOPP Bureau, this deficiency is due to an existing vacant position that was not filled during our audit period, and miscommunication within the AOPP Bureau as to who was to be performing this process.

The Contract Manager's Handbook, dated June 2007, Chapter 4, Invoice Process, page 16, specifies:

The first week of every quarter Accounting Operations and Tax Bureau (AOTB) sends a Contract Verification Memo to every Lottery Contract Manager. The memo must be reviewed/approved and returned to AOTB approximately 2 weeks from the date of the memo. This ensures that the available balance for the contract is the same on both the Contract Manager's and AOTB's contract payment logs. This also ensures that the Contract Manager has seen all invoices paid against the contract and helps to verify that AOTB has received and paid all invoices which have been approved by the Contract Manager.

The lack of reconciliation between contract manager's payment records and the official accounting records increases the chance of inaccurate and incomplete total invoices, and an incorrect contract balance. Without correct balances, the contract manager could not effectively monitor the contract by ensuring that financial commitments did not exceed the maximum amounts payable under the contract.

Recommendation

In order for the Lottery to effectively monitor the financial obligations under its contracts, it should perform quarterly reconciliations between the contract manager's payment records and the official accounting records, according to procedures delineated in the Contract Manager's Handbook. In addition, the Lottery's AOPP Bureau should assign staff who will be performing quarterly payment reconciliation process to ensure memos will be prepared, sent, and returned in a timely manner.

Lottery's Response

The Lottery agrees with the finding. The Lottery is currently performing quarterly reconciliations for all active contracts and will complete its quarterly reconciliations two weeks after the end of each quarter.

SCO's Comment

The Lottery concurs with the finding and recommendation.

**Attachment—
California Lottery's
Response to Draft Report**

600 North Tenth Street
Sacramento, CA 95811
calottery.com



March 24, 2011

Jeffrey V. Brownfield, Chief
Division of Audits
State Controller's Office
Post Office Box 942850
Sacramento, California 94250-5874

Re: 3 BALL PRODUCTIONS/MILESTONE ENTERTAINMENT CONTRACT

Dear Mr. Brownfield:

The California State Lottery (Lottery) offers the following general comments and specific points regarding the recently concluded audit conducted by the State Controller's Office (SCO). The audit scope was limited to an audit of the Lottery's fiscal controls over the monitoring of the 3 Ball Productions/Milestone Entertainment contract.

The draft report lists five recommendations for the Lottery to consider. The Lottery appreciates these recommendations and has implemented corrective actions after being notified of deficiencies during the audit.

Below are the Lottery's responses to the specific recommendations provided in the draft audit report. The Lottery will develop a work plan as part of the SCO follow-up process.

FINDING 1 - The Lottery improperly overpaid an advance payment and lacked support for contract expenditures.

RECOMMENDATION:

The Lottery should properly verify contract expenditures to the contract's terms and conditions to ensure advance payments are made at the percentage allowed. In addition, the Lottery should recover any payments that were not adequately supported. In the future, the Lottery should obtain and review supporting documentation to ensure expenditures are proper and accurate before payments are processed.

RESPONSE:

The Lottery agrees with the finding and took immediate corrective action in July 2010 by assigning a new contract manager and emphasizing internal controls over contract payments. Currently, contract expenditures are verified to contract terms and advance payments are made at the percentage allowed. The Lottery initiated a formal dispute on unsupported costs and will seek to recover disputed payments.

Jeffrey V. Brownfield
March 24, 2011
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FINDING 2 - A contract payment was made before the amendment authorizing the additional funding was executed.

RECOMMENDATION:

The Lottery should not authorize additional contract work or expenses until a contract amendment is fully executed. The Accounting Operations and Prize Payment Bureau should not pay for any work performed except as authorized under the contract.

RESPONSE:

The Lottery agrees with the finding and will ensure that future contract work or expenses are not authorized until a contract amendment is fully executed. In addition, the Lottery will ensure payments are made for work performed under the contract.

FINDING 3 - The Lottery failed to follow approved competitive bidding guidelines.

RECOMMENDATION:

The Lottery should properly oversee contracts by monitoring the competitive bid procedures for purchases of more than \$100,000. These procedures are designed to ensure that the Lottery gets the best price possible. In addition, if the Lottery does not use the competitive bidding process, the director must prepare a memorandum explaining why the competitive bidding process is not being used, and send it to the Chairman of the Commission.

RESPONSE:

For clarification, the Lottery's competitive bidding guidelines allow the Director and prime contractors to procure goods or services without utilizing competitive procedures if the goods or services are being acquired through a subcontract to a competitively bid prime contract that identified the goods or services at the time of prime contract award. The scope of services in the Request for Proposal for the "Make Me a Millionaire" game show required the contractor to provide studio equipment and a set design including the procurement of game set pieces and lighting. Because the studio equipment and set design are part of the prime contractor's scope of work, the Lottery considers that the game set pieces and lighting to have been competitively bid by the prime contractor, in accordance with the Lottery's competitive bidding regulations.

The Lottery's competitive bidding guidelines are complex and are relevant only in the context of a state-operated lottery. To ensure a consistent application of its guidelines the Lottery will provide consultation and training to contract managers as needed to ensure its guidelines are followed. Based on this clarification, the Lottery respectfully disagrees with the finding.

Jeffrey V. Brownfield
March 24, 2011
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FINDING 4 - Improper use of the office revolving fund.

RECOMMENDATION:

The Lottery should only use the office revolving fund process for purposes as delineated in SAM, and payment of contract expenditures should be paid through the normal claim processing procedure and a State Controller's warrant issued.

RESPONSE:

The Lottery agrees with the finding. The Lottery will comply with its existing payment procedures by processing claims through SCO for contract expenditures and will use the office revolving fund in accordance with SAM guidelines.

FINDING 5 - Payment reconciliations were not performed consistently.

RECOMMENDATION:

In order for the Lottery to effectively monitor the financial obligations under its contracts, it should perform quarterly reconciliations between the contract manager's payment records and the official accounting records, according to procedures delineated in the Contract Manager's Handbook. In addition, the Lottery's AOPP Bureau should assign staff who will be performing quarterly payment reconciliation process to ensure memos will be prepared, sent, and returned in a timely manner.

RESPONSE:

The Lottery agrees with the finding. The Lottery is currently performing quarterly reconciliations for all active contracts and will complete its quarterly reconciliations two weeks after the end of each quarter.

If you have any additional questions, please contact my Audit Chief, Roberto Zavala at (916) 323-7156.

Sincerely,



Linh Nguyen
Acting Director

**State Controller's Office
Division of Audits
Post Office Box 942850
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